

Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred incident to sales of service. See 86 Ill. Adm. Code 140.101. (This is a GIL.)

July 27, 2007

Dear Xxxxx:

This letter is in response to your letter dated November 27, 2006, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.ILTAX.com to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

Background and Facts

Our client ('Taxpayer') is engaged in the business of selling advertising and marketing services to unrelated third parties ('Advertiser'). The Taxpayer has recently entered into advertising/marketing agreements to distribute beverage cup sleeves bearing third party advertisements approved by the Advertiser to Cafés and other similar establishments ('Cafés'). All advertisements are in the form of text and/or graphics printed on the beverage cup sleeves provided by the Taxpayer to the Cafés. The printed advertisements comprise predominantly the entire beverage cup sleeve. The Advertiser has final approval for all of the printed advertisements and artwork on the beverage cup sleeves before they are distributed to the Cafés.

Taxpayer's Agreement with the Advertiser

The Taxpayer is the purchaser and owner of the beverage cup sleeves inventory and does not sell the beverage cup sleeves to the Advertiser purchasing the advertising and marketing services. The Advertiser is required to reimburse the Taxpayer based on a per unit quantity of beverage sleeves distributed to the Café displaying its approved advertising messages. The Taxpayer purchases the raw materials and other printed advertising materials for final assembly at its manufacturing operations located in California and Nevada. After final assembly, the Taxpayer distributes the hot beverage

cup sleeves bearing the sales message of the Advertiser to the Cafés by common carrier. The Cafés receive the advertising free of charge and become the owner of the beverage cup sleeves (i.e., printed materials). The agreement with the Advertiser requires that the Taxpayer or its representative monitor the Café to confirm that the Café is distributing the beverage cup sleeves to its customers during the term of the advertising agreement. Confirmation that the Café is distributing the beverage cup sleeves to its customers may occur via telephone or an in-state visit by the Taxpayer or its representatives.

Taxability of the Printing and Distribution of Beverage Cup Sleeves

Given that the Taxpayer has a taxable presence in your state and that its customers (i.e., Cafes) are located in your state, does the sale of the advertising services described above qualify as a direct mail or printed sales message in your state? If so, is the printed sales message described above subject to sales or use tax in your state?

Should you have any questions, please contact PERSON.

DEPARTMENT'S RESPONSE

Without further information and review of the contractual obligations of the parties, we cannot provide more specific answers. However, we hope that the following general information is useful.

When a printing company contracts to print custom printed marketing literature, a special order printing situation exists and liability is incurred under the Service Occupation Tax Act. Who is liable for the tax in these situations depends upon the method chosen by the printer in calculating his Service Occupation Tax liability. See 86 Ill. Adm. Code 130.2000 and 140.101.

Retailers' Occupation Tax and Use Tax do not apply to receipts from sales of personal services. Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred incident to sales of service. For your general information see 86 Ill. Adm. Code 140.101 regarding sales of service and Service Occupation Tax.

The purchase of tangible personal property that is transferred to service customers may result in either Service Occupation Tax liability or Use Tax liability for the servicemen, depending upon which tax base the servicemen choose to calculate their liability. Servicemen may calculate their tax base in one of four ways: (1) separately stated selling price; (2) 50% of the entire bill; (3) Service Occupation Tax on cost price if they are registered de minimis servicemen; or, (4) Use Tax on cost price if the servicemen are de minimis and are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of sales of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If servicemen do not wish to separately state the selling price of the tangible personal property transferred, those servicemen must use the second method where they will use 50% of the entire bill to their service customers as the tax base. Both of the above methods provide that in no event may the tax base be less than the cost price of the tangible personal property transferred. Under these methods, servicemen may provide their suppliers with Certificates of Resale when purchasing the tangible personal property to be transferred as a part of the sales of

service. Upon selling their product, they are required to collect the corresponding Service Use Tax from their customers.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). See, 86 Ill. Adm. Code 140.101(f) enclosed. This class of registered de minimis servicemen is authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to sales of service. Servicemen that incur Service Occupation Tax collect the Service Use Tax from their customers. They remit the tax to the Department by filing returns and do not pay tax to suppliers. They provide suppliers with Certificates of Resale for the property transferred to service customers.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). Such de minimis servicemen may pay Use Tax to their suppliers or may self-assess and remit Use Tax to the Department when making purchases from unregistered out-of-State suppliers. Those servicemen are not authorized to collect "tax" from their service customers because they, not their customers, incur the tax liability. Those servicemen are also not liable for Service Occupation Tax. It should be noted that servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis.

The Department has recognized situations where printed materials are "used" outside Illinois and then placed for mailing by mail or common carrier outside Illinois for delivery into Illinois, and during which, the serviceman loses the ability to exercise control over the printed materials (e.g., to recall the materials). See for example ST 06-0004-PLR, ST 01-0166-Gill, and ST 01-0003-GIL. Generally, in those situations, a serviceman would not incur a Use Tax liability nor a Service Use Tax collection obligation if the serviceman does not retain the ability to exercise control over the shipment of the printed materials after entry into Illinois. This letter and the general information letters referenced above also describe the general tax liabilities of printers in special order printing situations. Such liabilities may accrue, if the serviceman were to have any control over the printed materials in this State.

If you require additional information, please visit our website at www.ILTAX.com or contact the Department's Taxpayer Information Division at (217) 782-3336. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Very truly yours,

Martha P. Mote
Associate Counsel